

CHAPTER TWO: THEORETICAL FRAMEWORK AND LITERATURE REVIEW ON PRIVATISATION

2.1. Introduction

The involvement of the private sector in the provision of public services has always been linked to the process of globalisation and more specifically with that of neoliberal globalisation. Thus, (whether it concerns a public-private partnership or a full privatisation) the analysis should be done with consideration of the global phenomena that may be behind it or underpinning it. This chapter defines the key concepts involved in privatisation and highlights the relationship between privatisation and neo-liberal globalisation.

2.2. Neo-liberal globalization

2.2.1. Definitions and discussions

Globalization can be defined as an extensive integration of production, trade, finance, and information across states and societies such that the economic, cultural, and often political consequences of actions in these realms become increasingly undifferentiated and impact each other across national and regional boundaries (Massamba *et al.* 2004). Shortly, given the movements and counter movements that interact worldwide, it can be argued that globalisation is broad, inclusive, multi-faceted and contradictory.

While much literature conflates globalisation and neo-liberalism this study sees the two as separate things. In fact globalisation is not a recent phenomenon. It started way back for centuries when Europeans began to migrate from Europe to other continents either for colonisation or for other purposes ending up with conquering other places and people (O'Rourke and Williamson 2000).

However, neo-liberalism is a set of economic policies that have become widespread during the last 1980s. According to Martinez and García (2000), it is a philosophy in which the existence and operation of the market are valued in and of themselves (market fundamentalism), and where the operation of a market or market-like structure is seen as an ethic in itself, capable of acting as a guide for all human action, and substituting for all other existing ethical beliefs. Neo-liberalism was promoted mostly under the era of Reagan in US and Thatcher in the UK, and around the world it has been supported or

imposed by powerful financial institutions like the International Monetary Fund and the World Bank (Held *et al.* 1999).

Thus, neo-liberal globalisation refers most commonly to the dramatic increase in the number and variety of transnational economic transactions, foreshadowed in the years leading up to World War I (Held *et al.* 1999). In addition, the process of adapting to global conditions requires adjustments on the part of both producers and consumers which is precisely why globalization is often viewed as the worldwide convergence of supply and demand. In short, neo-liberal globalization can be thought of as the widening, intensifying, speeding up, and growing impact of world-wide interconnectedness with the predominance of the market. In most cases it refers to the increasingly rapid movement of goods, services, capital, people and information around the world. However, when people debate globalization, they most often refer to policy choices, not technological advances. It is these policy choices that spark the real debate.

In fact, as barriers to trade have fallen across the world, markets for goods and services have become global and national economies have increasingly entered into global competition. The primary issue is that even if national economies can gain from increased international trade, the gains are highly uneven. Thus, there are clear winners and losers, both between and within countries. From this point of view, economic globalization serves merely to global inequalities. In fact, as Wilson (2004) observes, the neo-liberal agenda advanced through structural adjustment programs generally involves cuts in government spending, strong promotion of exports, privatization of public enterprises, currency devaluations, high interest rates, strict control of credit and money supply, removal of controls on trade and exchange, and deregulation of wages and prices (O'Brien and Leichenko 2003 and Williamson 2002).

In describing and explaining the dynamic of globalization Lubbers and Koorevaar (1998) insists its prime movers to be the following:

- (1) technological innovation (which has such an impact on mobility and communication that the 'technological revolution' implies a 'social revolution' and a decisive shift from industrial capitalism to a post-industrial conception and reality of economic relations)

- (2) the hegemony of the neo-liberal ideology (about the triumph of the market-ideology, the economization and commoditisation of life, mass-consumption and entertainment, deregulation).

Neo-liberalism has become a global ideological breakthrough (neo-liberal hegemony) in which democracy is considered to be a twin of the market-economy and these together are supposed to form a winning team (Lubbers and Koorevaar 2000, Robinson 2004).

Hegemony, as used by Gramsci, denotes the predominance of one social class over others (e.g. bourgeois hegemony). This represents not only political and economic control, but also the ability of the dominant class to project its own way of seeing the world so that those who are subordinated by it accept it as common sense and natural (Cammett 1967). In terms of hegemony the general consensus is that there is only one sensible way of seeing the world and any groups who present an alternative view are therefore marginalized.

In Gramsci's analysis, apart from violence and political coercion (used primarily in dictatorial regimes), another crucial element to maintain power is to construct hegemony through the successful adoption of the ruling class ideology by the oppressed or working class (Cammett 1967, Pillay 1996). Thus, the supremacy of a social group manifests itself in two ways, as domination and as intellectual and moral leadership; and the normal exercise of hegemony on the now classical terrain of the parliamentary regime is characterised by the combination of force and consent, which balance each other reciprocally, without force predominating excessively over consent. That's how Gramsci comes to argue that for real change to occur the dominated classes must move from a war of maneuver (confrontation with dictatorial regimes) to a war of position (counter hegemonic ideas) (Cammett 1967, Pillay 1996, Robinson 2004, Wilson 2004).

Lubbers and Koorevaar (2000) admit that there has been and still is an enormous interaction between technological and ideological globalization and it is this interaction which has led to the globalization of the neo-liberal economy. The hegemony of neo-liberalism became especially visible after the Cold War and became more convincing with the fall of the Berlin wall in 1989 and the collapse of the USSR in 1991 (Robinson 2004, Wilson 2004). Clearly then, it is both ideas and structure (economic and technological

developments and turbulences) that caused neo-liberal globalization. Therefore, the world is forced into neo-liberal globalization mostly by technology and the accepted ideology. It is by this ideology that people forced themselves into the process of internationalization thus creating a more and more borderless world, less and less characterized by territories as a consequence a new geography of power (Held 1999).

The internationalization of economic processes, both in production and consumption, the consequent emergence of a world market and Transnational Corporations (TNCs), worldwide capital flows, growing economic interdependence between countries and so on may have given birth to globalization. With borders ceasing to be meaningful and states losing power to economic actors (Boggs 2002) the dynamic of the free world market may have forced countries into globalization (Robinson 2004). But the internationalization of economic life could not have gained so much strength without state policies and policies of intergovernmental organizations supporting it (Boggs 2002, Held 1999, Lubbers and Koorevaar 1998).

The neo-liberal ideology has invited policymakers to liberalize markets, to deregulate economies and to privatize state-firms. Under systems of neo-liberalism, producing, selling and buying are less confined to actual geographic markets and production places; lending and borrowing, investing and speculating have become 'around the globe' activities (Boggs 2002, Held 1999, Wilson 2004). In accepting neo-liberal ideology people have acted in accordance with it to the extent that the world itself came to work according to the logic of that ideology. Actually, neo-liberal globalization demands efficiency, accelerates technological change and forces societies and individuals to adapt economically, politically, and psychologically (Lubbers and Koorevaar 1998); but it rewards those who are prepared for it and punishes those who are not; undermines traditional forms of national sovereignty and causes citizens to fear loss of control (Boggs 2002).

The consequences of globalisation follow from the fact that the traditional tasks of states are being less fulfilled, because states, by acting in accordance with neo-liberal ideology and in adapting to globalization, have transformed themselves from Keynesianism (protecting the national public good) to neo-liberalism more oriented on the international private capital in the worldwide market system (Lubbers and Koorevaar 1998).

Furthermore, since the globalization process has now gained strength of itself, states are also becoming objectively less powerful not only for fulfilling traditional social tasks like redistributing welfare and protecting the environment, but also less capable of fulfilling tasks necessary for international capital itself: securing property-rights, ownership and social order, fighting criminality and safeguarding peace (Lubbers and Koorevaar 2000).

The capacity for governance and the will to govern is diminishing and this causes four 'governance deficits': social deficit (international fairness and job issues), democratic deficit (national and international democratic imbalances), ecological deficit (environmental deterioration) and security deficit (threats to the global order) (Lubbers and Koorevaar 1998). But according to Martin Wolf⁶ 'globalization does not force governments to disappear; it forces them to take the interests of their most valuable assets, their skilled and entrepreneurial people into account' (cited Schirmer and Bernstein 2005:23).

While assuming that governments are indeed an essential aspect of a market-based system and have a vital role to play in taking global market opportunities, Wolf emphasizes that the state is now more omnipresent than ever before. The fact is that states do regain some of their governance-capacity by pooling authority on a higher geographical level, in regional political institutions and in International Governance Organisations (IGOs), but the governance capacity and the will to govern are diminishing and this threatens the quality of life in the globalizing world in several ways, particularly causing governance deficits (a social, democratic, security and ecological deficit) (Boggs 2002, Williamson 2002, Wilson 2004).

Boggs (2002) insists that globalisation has culminated in massive social dislocations, growing inequality, harsh consequences of the sort mentioned above, and increasing disconnection between centers of economic decision-making and political forms that historically nourished local participation and democratic citizenship. He argues that in the 'age of neoliberal hegemony everything winds up subordinated to the laws and dictates of the international market' (Boggs 2002:20), whilst the concerns of labor, health, human rights, and the environment are pushed beyond the reach of public discourse and intervention.

⁶ Wolf M (2004), *Why Globalisation Works*, Yale University Press, New Haven

2.2.2. The role of International Financial Institutions in neo-liberal globalisation

According to Peet (2003) globalisation has been accompanied by the growth in power of a few prodigious institutions operating under principles that are decided upon undemocratically, and that drastically affect the lives and livelihoods of a world of peoples. As Peet says: ‘When the USA bound itself to international commitments, it did so from a pre-eminent position, and insured that the commitments made conformed to American interests’ (Peet 2003:38).

The United States viewed multilateral institutions as instruments of foreign policy to be used in support of its specific interests. To all intents and purposes the global governance institutions have been and still are dominated by the American will. Peet (2003) observes that within these global governance institutions there is a growing influence of a single ideology, neoliberalism. He notes that the IMF, WB and WTO are all agents of a dominating centre of hegemonic power. Peet (2003:38) observes

‘In tracing how policies come to be widely adopted, most importantly by global governance institutions, we thought that investigation should focus on clusters of related economic and political institutions. These clusters of institutions are the agents that concretely carry out the production of scientifically legitimated policy prescriptions on behalf of power interests’.

The International Financial Institutions (IFIs) are instrumental, in this regard, through their neo-liberal policies that restrict debates and options on policy especially for developing countries. Even if the IFIs are facing a crisis of legitimacy mainly around the lack of democracy in policy-making (also their double standards) and the inappropriateness of their policies that are not addressing the continuing economic crises experienced worldwide, counter-hegemonic forces have not been able to change the *status quo* ‘Washington Consensus’, about the ‘need’ for national governments to adopt ‘sound economic fundamentals’ like trade and financial liberalization, privatization, deregulation, less state intervention, government budget cuts and labor flexibility to achieve development (Van Rooyen 2002).

The hegemony formed by the alliance of these institutions is founded on the speculation of the market. According to Peet, in the absence of an overriding ideology, these institutions would not have the homogeneity and self-confidence necessary for imposition and influencing international economic policy. It is formed through interactions of three kinds of institutional actor – bureaucratic, economic and political. What is particularly

fascinating about the hegemony of these institutions is that, apart from the influence of politics and economics by governments of the leading capitalist countries dominated by the USA, there is also an academic connection common to all these institutions. The academic connection from elite universities like Harvard University, especially their economics departments, business and law schools, all put a scientific stamp on the theoretical knowledge that underlies economic policies (Goldman 2004, Peet 2003, Ruckert 2005, and Van Rooyen 2002).

Through structural adjustment lending, the IFIs have been able to put pressure on developing country governments to open up their economies to transnational capital and to direct their economies towards export-orientation. It is this argument that leads Ruckert to say that 'International Financial Institutions have the function of co-opting elites from the periphery and absorbing counter-hegemonic ideas to ensure the dominance of the hegemonic ideology' (Ruckert 2005:5). The IMF and World Bank use the weapon of debt reduction to enforce the contemporary global economy - devising economic policies that will guarantee continued domination of the already - powerful interests, while coming up with claims that these policies are the cure for countries in economic distress (Peet 2003, Ruckert 2005).

According to Nuruzzaman 'While the World Trade Organisation is engaged in the task of eliminating all barriers to global free trade, the World Bank and the International Monetary Fund look after the liberalization of domestic capital accounts and privatization of the economies in the Southern developing countries' (Nuruzzaman M. 2001:3). The IMF, World Bank and WTO impose a virtually synonymous set of neo-liberal economic policies on countries all over the world. These policies are imposed as conditions for loans in terms of crisis, as qualifications for debt relief, as part of development assistance for countries much in need and as requirements for membership in vital international trade agreements (Goldman 2004, Peet 2003).

Ruckert (2005) considers that for all these International Financial Institutions, sound macroeconomic policies consist of trade and financial liberalization, privatization, fiscal prudence and low inflation, civil service reform and deregulation of labour markets. It is from this theoretical perspective, that the International Financial Institutions are seen as important actors in the neoliberal restructuring of the capitalist world economy towards a

transnationally oriented regime of accumulation, leading to global circuits of capital accumulation (the hegemony of a transnational elite representing transnational capital).

2.3. Privatisation

2.3.1. What does privatisation mean and why privatisation?

Privatisation - a search for definitions

The word 'privatisation' has attained global popularity in the last two decades. Several authors have attempted to define it. According to Bailey, privatization '(...) might be tentatively defined as a general effort to relieve the disincentives towards efficiency in public organizations by subjecting them to the incentives of the private market (Bailey, 1987:138 quoted by Aktan, 1991:1)

In the opinion of Aktan (1991), privatization refers, broadly speaking, to the transfer of functions previously performed exclusively by the public sector, to the private sector. It is an umbrella term which encompasses all methods or policies implemented to increase the role of market forces within the national economy. In this context, the concept of privatization covers several arrangements to deliver goods and services by the private sector (Aktan 1991).

For Starr (1998), privatization is a fuzzy concept that evokes sharp political reactions. He argues that privatization covers a great range of ideas and policies, varying from the eminently reasonable to the wildly impractical. According to the same author, privatization primarily means two things: first any shift of activities or functions from the state to the private sector; and, more specifically, any shift of the production of goods and services from the public to the private. He argues that besides directly producing services, governments establish the legal frameworks of societies and regulate social and economic life, and they finance services that are privately produced and consumed. Another author, Savas (1987) defines privatisation as the act of reducing the role of the government, or increasing the role of the private sector, in an activity or in the ownership of assets.

Privatisation can be defined as denationalization, which refers to the sale of assets or shares of a publicly owned enterprise to the private sector. It may be more appropriate to talk of privatisation when the state transfers more than 50% of the shares of a state-owned

enterprise to the private sector. In this case, transfer of ownership (sale of shares) results in transfer of management and operation as well. However, full privatisation requires that all shares and assets of a state-owned enterprise must be sold to the private sector.

Why privatize?

In general, nations privatize state-owned enterprises to achieve one or more of several objectives such as raising revenue for the state; raising investment capital for the industry or company being privatized; reducing government's role in the economy; promoting wider share ownership; increasing efficiency; introducing greater competition; and exposing firms to market discipline.

Supporters of privatisation

Kodras (1997) argues that (at least in theory) privatization helps establish a 'free market', as well as fostering capitalist competition, thus providing the public with greater choice at a competitive price. The supporters of privatization thus argue that market competition increases efficiency and service quality.

Bach (2000) affirms such a belief arguing that public enterprises are inefficient because they are operated to pursue certain objectives (e.g. excess employment), to satisfy the political parties. After privatization, the cost for politicians to intervene in the firm in order to promote their personal goals becomes prohibitively high, because privatization drives a wedge between the manager and the politician. The politician may find it unprofitable to convince the manager not to undertake restructuring to maintain excessive employment. Hence, Bach (2000) believes, privatization can render firms more efficient by controlling the politician's discretion.

Bennett (1990) and Boyne (1996) advocate that governments run business poorly for reasons of lack of performance, corruption, political influence, mismatch between the role of the government and business interest. The basic argument given is that governments have few incentives to ensure that the enterprises they own are well run while private owners do have such an incentive (they will lose money if businesses are poorly run). Their theory holds that not only will the enterprise's clients see benefits, but as the privatized enterprise becomes more efficient, the whole economy will benefit.

Another argument for privatization is that to privatize a company, (which was non-profitable or even generated severe losses when state-owned) means taking the burden of financing it off the shoulders and pockets of taxpayers, as well as free some national budget resources, which may be subsequently used for something else (Sheshinski and López-Calva 1999). As Sheshinski (1999) maintains that it is both unethical and inefficient for the state to force taxpayers to fund business that cannot work for itself. Sheshinski (1999) holds that even if the privatized company happens to be worse off, it is due to the normal market process of penalizing businesses that fail to cope with the market reality or that simply are not preferred by the customers.

Arguments against privatisation/pro government

Arguing against privatisation Kodras (1997) challenges the claims concerning the alleged lack of incentive, saying that governments have to ensure that the enterprises they own are well run, as they must answer to the people. He argues that a government, which runs nationalized enterprises poorly, will lose public support and votes, while a government, which runs those enterprises well, will gain public support and votes. Thus, democratic governments do have an incentive to maximize efficiency in nationalized companies, due to the pressure of future elections. Kodras recognizes that competition in service provision is often absent, resulting in monopoly rather than greater efficiency. Kodras (1997) believes that it is undesirable to involve private entrepreneurs in providing essential services such as water, electricity, health, education and so forth because the driving motive of a private company is profit, not public service. He argues that the public welfare shouldn't be sacrificed to the demands of profitability and concludes that essential services should be left in public hands (Kodras 1997).

Starr (1987) notes that profits from successful private enterprises tend to end up in private pockets, rather than being made available for the common good. It is of concern that if a government-owned company is privatized, its new owner(s) could stop providing this service to those who are too poor to pay, or to regions where this service is unprofitable. Starr (1987) reveals that nationalized industries are usually guaranteed against bankruptcy by the state. They can, therefore, borrow money at a lower interest rate to reflect the lower risk of loan default to the lender. This however, does not apply to private industries. In cases where public services or utilities are privatized, this can create a conflict of interest between profit and maintaining a sufficient service. A private company may be tempted to

cut back on maintenance or staff training, to maximize profits. A public service may provide public goods that, while important, are of little market value (Starr 1987). Young (2004:16) summarizes arguments against privatization as follows:

‘privatisation does not save taxpayers' money; does not guarantee market competition and can result in private monopolies; leads to corruption and causes policymakers and managers to lose control over privatized services; diminishes accountability of government; private gain and public good do not always correspond; is unnecessary given other productivity approaches available to public service providers; compromises quality because of private vendor profit motive; lowers state employee morale; contributes to fear of displacement; destabilizes economically marginal communities’.

2.3.2. Privatization and neo-liberal globalisation

The meaning of privatization depends, in practice, on a nation's position in the world economy. In the wealthier countries it is easy to treat privatization purely as a question of domestic policy. But, where the likely buyers are foreign, as in the Third World, privatization of state-owned enterprises (SOEs) often means denationalization, in other words, a transfer of control to foreign investors or managers. Since state ownership, often originally, came about in an act of national self-assertion, privatization appears to be a retreat in the face of international pressure (Starr 1988).

Privatization has been driven by the increasing globalization of the world economy. Several decades of rapid growth in international trade and investment have made competitiveness in international trade an essential factor in a nation's ability to create jobs, raise real wages, and generate wealth. For many nations, privatization has become the only or most effective method of raising investment capital on favorable terms. High levels of past public sector borrowing have saddled many nations with large levels of debt. As a consequence, these nations have had little alternative but to sell state assets to reduce debt, generate revenue, and raise investment capital.

Besides, privatization has been a key component of structural reform programs in both developed and developing economies. As Hall (2004) observes, at the centre of these policies are the IMF and the World Bank. IMF loans are tied to countries' poverty reduction strategy programmes (PRSPs), which contain commitments to a range of policies, frequently including some form of privatisation. Poverty Reduction Strategy Papers (PRSPs) are subjected to the approval of the IMF and World Bank boards. This policy conditionality has a wide impact as support is tied to policies, which change the

structure of an entire sector (e.g. the privatisation or liberalisation of electricity systems). The World Bank's country assistance strategies (CASs) function in the same way, as a core set of policy conditions to which other World Bank aid is linked (Hall *et al.* 2004).

2.3.3. Public-Private Partnership

According to the Canadian Canadian Ministry of Municipal Affairs (1999), Public-Private Partnerships (PPPs) are arrangements between government and private sector entities for the purpose of providing public infrastructure, community facilities and related services. Such partnerships are characterized by the sharing of investment, risk, responsibility and reward between the partners. The reasons for establishing such partnerships vary, but generally involve the financing, design, construction, operation and maintenance of public infrastructure and services (Canadian Ministry of Municipal Affairs 1999, Pillay 2002). The underlying logic for establishing partnerships is that both the public and the private sector have unique characteristics that provide them with advantages in specific aspects of service or project delivery. The roles and responsibilities of the partners may vary from project to project. In some projects, the private sector partner may have significant involvement in all aspects of service delivery, in others, only a minor role.

While the roles and responsibilities of the private and public sector partners may differ on individual servicing initiatives, the overall role and responsibilities of government do not change. Public-private partnership is one of ways of delivering public infrastructure and related services. It is not a substitute for strong and effective governance and decision making by government. In all cases, government remains responsible and accountable for delivering services and projects in a manner that protects and furthers the public interest (Canadian Ministry of Municipal Affairs 1999).

The notion of partnership between the state, capital and civil society has taken on different forms over the decades (Pillay 2002). One of the Public-Private Partnership forms that are mostly used for utility provision is the management contract. Under this arrangement, the government contracts out with the for-profit, as well as not-for-profit organizations, for the delivery of goods and services. In other words, the government purchases services from a private firm or a non-profit organization. Contracting-out is common, especially in such services as public works and transportation, public safety services, health and human

services, parks and recreations services. Increasingly, municipal governments are interested in contracting such goods and services with private firms (Savas 1987).

2.4. International comparison of utility privatisation: some case studies

Over the past twenty years, the focus of development policy has shifted from the state to the private sector. Privatisation is now central to utility reform in much of Sub Saharan Africa. Thus, several studies on the impact of utilities' privatisation (such as water and electricity) have been conducted with different findings. This section provides a range of studies carried out on privatisation of utilities.

2.4.1. Sub-Saharan Africa

Until 2002, water privatisation had been carried out, to some degree, in at least fourteen countries in the region of Sub Saharan Africa (SSA), and many other governments were at various stages in the privatisation process (Bayliss 2002). However, in some cases privatisation has been difficult to achieve, and only few countries have successfully provided water under public ownership. As Bayliss (2002) says, evidence on the impact of privatisation indicates that the performance of privatised utilities has not changed dramatically, but that enterprises have continued to perform well, or not so well, depending both on their state when they were privatised and on the wider economic context. The evidence points to internal improvements in terms of financial management. However, governments face considerable difficulties in attracting investors and regulating private utilities.

Furthermore, privatisation fails to address some of the fundamental constraints affecting water utilities in Sub Saharan Africa, such as finance, the politicised nature of service delivery, and lack of access for the poor (Bayliss 2002). In most water and electricity supply contracts, the government retains responsibility for ownership and capital investment while the investor is responsible for operation and management of the services. Hall *et al.* (2002) observes that management contracts are being commonly used as a way of giving multinationals risk-free business in water, while smoothing the way for eventual lease or concession privatisation.

Bayliss (2002) assumes that although widely promoted across Sub Saharan Africa, privatization is difficult and costly to achieve in practice and the results may be limited. She observes that privatisation may bring little in the way of finance from investors beyond equipment for financial management. Furthermore, much of the money associated with privatisation comes from donors through the release of aid funds and this distorts the perspective of the policy. She believes that Gabon, Guinea and Senegal provide useful examples of where the public sector can be an effective provider of water. While reform efforts have sometimes met with failure, the case of Guinea demonstrates that privatisation cannot be expected to transform an enterprise.

Given the widespread weakness in regulation of the water sector in Sub Saharan Africa, Bayliss (2002) concludes that some alternative means of accounting for the performance of Multinational Corporations (MNCs) in the water sector in poor countries is required. The conventional approach to regulation pre-supposes a capacity and a bargaining position, which is often absent in many low-income economies. Bayliss (2002) suggests that where MNCs are supplying water – an essential service – to some of the poorest in the world, it is important to know that consumers are not being exploited. Companies need to be required to publicly disclose details of their operations in poor countries including information on turnover, profit, number of connections, average price charged, capital expenditure, transactions with parent company and outstanding debts. This information should enable policy makers in the host country and those proposing privatisation elsewhere to assess whether and how any efficiency gains have been achieved.

In Uganda, privatisation of SOEs was initiated in 1993 and, according to Ddumba-Ssentamu and Mugume (2001), it was really necessary given the appalling state of SOEs and their negative effects on the economy. Even if for many Ugandans the understanding is that privatisation was just a sale imposed on the country by Bretton Woods institutions to enrich government officials and give foreign investors windfall profits as a way of recolonisation, Ddumba-Ssentamu and Mugume (2001) remark that it increased the supply of quality goods and services, mostly basic commodities; it increased industrial capacity and profitability and labour gains were recorded. However, they argue that low-income categories were hurt by the adjustments.

2.4.2. South Africa

In South Africa a number of studies have been undertaken following the privatisation of water services. Water privatization was implemented as part of government policy aimed at making people pay for the full cost of having running water in their homes (total cost recovery⁷) (McDonald and Pape 2002). In practice, total cost recovery may have caused more misery than development. In poor areas where privatization has been implemented, millions of people have been cut off because they could not afford to pay water bills that often made up 30% of their incomes (Pauw 2003).

However, according to former Department of Water Affairs and Forestry Director General, Mike Muller (2004), the Municipal Service Project (of which MacDonald is the Co-director) had given false information about water cuts. As he asserts, a HSRC survey had showed that water cuts had several reasons other than non-payment (such as repairs and management). The fact only 7,7% of the households whose supply was interrupted due to non-payment confirms the HSRC findings. The survey highlighted the fact that the highest interruption rates were in Limpopo (38%) and Mpumalanga (27%), provinces in which the Department of Water Affairs and Forestry was providing services to many communities almost for free, and with no deliberate cut-offs. According to the Minister of Water Affairs and Forestry, the main problem affecting people was not cut-offs for non-payment but the ability of service providers to keep the water running (*Mail&Guardian*, 25/06/2004). It should be noted that the South African government adopted a Public-Private Partnership and not full privatisation in the provision of services.

Nonetheless, according to Bond (2004), water prices increased by 300 % in many areas of South Africa due to the cost recovery principle. The seriousness of the matter was such that by 2003, some village, town, and city councils tried to cancel the contracts with the water multinationals. The predicament faced by urban councils is that they are contractually obligated to pay the debts to the multinational corporations.

KwaZulu-Natal and Johannesburg

In 2000, rural residents in KwaZulu-Natal had to pay for water that used to be free (connection fee and/or volumetric charges), but the reality was that most poor households

⁷ Cost recovery refers to the practice of charging consumers the full(or nearly full) cost of providing services such as water and electricity (McDonald and Pape 2002:17)

could not afford services payment. This led to cut-offs that forced residents to seek water from nearby polluted rivers and stagnant ponds. Within weeks, cholera broke out and claimed more than 250 lives, and caused more than 100.000 cases of illness. As a consequence, the government has spent millions of dollars to control the spread of the disease and to truck clean water to stricken areas (Public Citizens 2004).

Johannesburg city has faced similar dilemmas. Since it concluded a management contract with the Suez Company, there have been growing protestations by residents of townships such as Soweto and Orange Farm. Residents claim they cannot afford charges on services (Public Citizens 2004). Furthermore, cut-offs and evictions are expensive and politically sensitive enforcement weapons, and that is why service providers interested in cost recovery have moved towards the use of prepaid meters wherever possible (McDonald and Pape 2002). It should be noted that, according a Reuters journalist ‘pre-paid meters were banned in Britain because they produce silent disconnections among the poor’ (*Mail&Guardian* 18-24/06/2004).

McDonald and Pape (2002) thus believe that it may require a far more radical decommodification of resources like water and energy to ensure a fairer distribution of these public goods and to build a policy framework on something other than the principle of ‘*you get what you can pay for*’.

2.4.3. Six capital cities study

In their study Noll *et al.* (2000) apply economic and political theory to identify the potential problems and advantages of private operation, and evaluate the reform experiences in six large cities – Abidjan, Buenos Aires, Conakry, Lima, Mexico City, and Santiago. The first part of the paper argues that efficient operation of water systems is politically more difficult in cities in which the marginal supply price of water is steeply increasing and in which waste water creates large externalities. The data suggested that reform improved performance in all cases, but the improvements were far greater in cities in which neither of these problems was large. Moreover, reform process was able to progress furthest in cities in which both water and safe waste disposal were relatively inexpensive.

2.4.4. South America

Bolivia

In South America Bolivia provides an illuminating case study for the downside of water privatisation. In fact in 1999, the Bolivian government, following the World Bank advice, provided a subsidiary of the US-owned Bechtel Corporation a 40-year lease to run the Cochabamba water supply. More than half a million people in the area, most of them desperately poor, came to depend on Bechtel for water. Bechtel tripled the price. In fact, rate increases of 100% were the most common, while increases of 300% were reported. Families earning a minimum wage of \$60 per month, suddenly, faced bills of \$20 per month. Instead of wringing their hands, the Cochabamba populace staged a general strike, shutting down the city and forcing President Hugo Banzer to either declare martial law or concede. Banzer ordered troops to disperse protestors, and repressive forces wounded some 100 people and killed four. But protest intensified and threatened to spread, so Banzer conceded and broke the contract with Bechtel (Landau and Patel, 2005).

On the same Bolivian case, Bojanic and Krakowski (2003) agree with Landau and Patel's concerns that privatization improved water access for larger urban groups only while increasing the suffering of the rural poor.

Using household survey data, Barja and Urquiola (2001) have estimated, for urban areas, the changes in connection rates pre- and post-capitalization, for telecommunications, water and electricity, and found connection rates rose in all sectors, dramatically in telecom and water, and by a modest 2.9% in electricity (Barja and Urquiola 2001). Barja and Urquiola list four reasons why prices might rise following reforms: to meet cost-recovery and investment requirements; to make up for the disappearance of subsidies; to meet the costs of more formal revenue collection and the elimination of illegal connections and to deal with price shifts in substitutes or complements.

Argentina

In the 1990s, about 30% of water companies covering approximately 60% of Argentina's population were privatized (Galiani *et al.* 2002). In studying the impact of water privatization on child mortality rates in Argentina, Galiani used the variation in ownership of water provision across time and space generated by the privatization process. He concluded that child mortality had fallen 8% in the areas that privatized their water

services, and that the effect was largest (26 %) in the poorest areas (Galiani *et al.* 2002). Galiani *et al.* (2002) also found that while privatization was associated with significant reductions in deaths from infectious and parasitic diseases, it was uncorrelated with deaths from causes unrelated to water conditions. As Galiani *et al.* (2002) put it, the deterioration in performance of water systems in Argentina under public management was so large that this allowed for a privatization that generated private profits, attracted investments, expanded service, and reduced child mortality.

With regard to cost and quality of service, Galiani *et al.* (2002) showed that water use fees (e.g. in Buenos Aires) were initially lowered by 26.9% as a result of the privatization bid. However, thirteen months after privatization, the regulator authorized a 13.5% increase in the usage fee, and a significant increase in connection fees. The increase in the connection fee was controversial as it was very close to the monthly household earnings level for the official poverty line. In response to protests, the connection fee was quickly lowered and replaced with a small fixed charge that was added to the water use bills for all clients. This explicit cross-subsidy allowed the firm to reduce the connection fees to about one tenth of the previous levels. Galiani *et al.* (2002) found that the enforcement of service payment was toughened after privatization and that the private operator was allowed to cut service to customers with three unpaid bills (although it could be reconnected under the regulator's request).

Although in the early 1990s, with the new presidency of Carlos Saúl Menem, many thought the country was on the cusp of a great turn around privatisation was in fact a real failure (Bryant 2001). A combination of incompetence, corruption and hyperpresidentialism prevented the privatization regimen from benefiting the country as it ought to have. Indeed, the economic incentives were scarcely touched on, as the Argentine economy continued to falter and the individual sectors went from inefficient state monopolies to well-managed rent-seeking oligopolies and monopolies. The consequences included the fact that, on the domestic political level, Menem became highly disrespected, and on the international level, entities like the World Bank that once applauded Argentina's aggressive privatization stance disdained its blunderings.

Peru

According to Birdsall and Nellis (2002), a study by Torero and Pasco-Font in 2001, on the income distribution effects of electricity and telecommunications privatization and water sector reform in Peru, found that the privatized utilities expanded coverage dramatically in telecommunications, by 167% in five years, electricity customers increased by 1/3 in the first four years, following divestiture while there was less expansion of the reformed but not privatized water and sewerage services. According to this study, quality and reliability of all services increased greatly in the privatized firms, with more modest quality improvements in water.

On the other hand, prices rose significantly in all sectors, including water. Pre-sale and pre-reform tariff levels had not covered costs in any of the sectors. Investment, especially, had lagged under state ownership. Comparison of pre-sale and post-sale periods revealed higher access and better distribution (proportionately higher access gains of the lower income groups than the upper) of telecommunications services following sale, a slight progressive change in electricity, and almost no change in water and sewerage curves. The study indicated that consumer surplus declined, due mainly to price increases. Birdsall and Nellis (2002) concluded that the overall short-term distributional effects of privatization on income were slightly negative, but they varied by sector. Moreover, the post-sale tariff increases were required to cover financial charges and investment costs. To protect lower income consumers, the authors called for different tariffs according to family type and income level (Birdsall and Nellis 2002).

2.4.5. Europe, the case of Britain

In terms of prices and system reliability, the reforms in Britain appear to have been a success. The main factors were: 'reductions of 30-40 % in fossil fuel prices; temporary price reductions due to the effective write off of much of the pre-privatisation asset base; and a shift in nuclear liabilities away from the then generation to future generations' (Thomas 2002:2). However, even if the introduction of retail competition for large consumers allowed them to negotiate better prices, it seems that much of the price reduction was paid for by small consumers. The extension of retail competition to small consumers seems to have made the problem worse and has also given electricity companies an incentive to discriminate against poor consumers that did not exist while retail supply was a monopoly business (Thomas 2002).

2.4.6. Asia, the case of China, Indonesia, Malaysia, Philippines and Vietnam

Toba (2003) undertook a cost-benefit analysis of the privatisation of electricity in the Philippines. His study estimates significant benefits in the form of lower avoided costs and a positive impact on the state-owned utility. The results also indicate that only about one-quarter of the estimated gains to private investors was passed on to domestic investors.

A report commissioned by PSIRU⁸ in 2004, surveys the activities of multinational water companies in Asia. According to that report, the companies are struggling with existing contr

acts, have to withdraw from some national policies, and show no enthusiasm for expansion, except in China. The activities of Asian private companies in water lead to a conclusion that their international activities are so far limited, and mainly consist of joint ventures with multinationals. The experience of a number of countries in Asia highlights that problems continue to be experienced in countries which have made extensive use of private companies, such as Indonesia, Malaysia and the Philippines (Hall *et al.* 2004).

According to the abovementioned report, 'a number of water supply BOT (build-operate transfer) projects have been abandoned or are causing serious problems in Vietnam, China, Malaysia and elsewhere, due to unaffordable levels of prices being built into *take-or-pay* contracts' (Hall *et al.* 2004:3). Given that similar problems have been observed elsewhere in the world, the report suggests that there should be a serious re-appraisal of the economics of existing water supply BOTs, and a moratorium on further developments (Hall *et al.* 2004)

Public versus Private in Asia: comparatively favourable

Apart from that, the performance of public utilities in Asia compares well with that of the privatised operations in Jakarta and Manila. Actually, cities such as Osaka and Phnom Penh, run by effective public sector water operators, can clearly provide lessons for other water undertakings in Asia. Thus the report notes that this stands as evidence that private operators, despite all the financial and other support they had received, were no more likely to have extended services than cities without private operators. The report observes also that there has been an extremely high failure rate for private concessions and long-term BOT contracts, which may get worse if Suez and Thames leave their contracts in Manila and Jakarta (Hall *et al.* 2004).

⁸ Public Services International Research Unity (PSRU) is a Greenwich University based research unity

2.5. Conclusion

This chapter has revealed a clear connection between neoliberal globalisation and privatisation. As countries engage in the global arena so privatisation gains ascendance. American and Western hegemony plays a key role in the process of neo-liberal globalisation. Whether privatisation of utilities benefited nationals or foreigners is still a matter of debate as evidence shows different results in different case studies. In some countries utility privatisation failed to deliver to citizens while foreign privates might have benefited. However, in some other countries, utility privatisation is believed to have yielded positive results.